

Gary Gensler, Nominee for CFTC Chairman
Response to Senator Sanders
May 14, 2009

1. The CFTC should produce quarterly reports on its website describing the role derivatives trading activities have in influencing prices for each major energy commodity, including home heating oil and crude oil.

I believe that we must urgently move to enact a broad regulatory regime that covers the entire over-the-counter derivatives marketplace. This regime should consist of two main components. One component is the regulation of the derivatives dealers themselves. The other component is the regulation of the marketplace. I believe it is best that we implement both of these complimentary components to bring the needed transparency, accountability and safety to the trading of OTC derivatives.

Market efficiency and price transparency for OTC derivatives should be significantly enhanced by:

- requiring the clearing of standardized products through regulated central counterparty clearinghouses;
- moving the standardized part of these markets onto regulated exchanges and regulated, transparent electronic trade executions systems;
- requiring development of a system for timely reporting of trades and prompt dissemination of prices and other trade information;
- requiring that all OTC transactions, both standardized and customized, be reported to a regulated trade repository; and
- requiring clearinghouses and trade repositories to, among other things, make aggregate data on open positions and trading volumes available to the public and to make data on any individual counterparty's trades and positions available on a confidential basis to the CFTC and other regulators.

I also believe the CFTC should promote greater transparency by providing more useful and comprehensive data to the public. In my opinion, the rapid growth in commodity index funds was a contributing factor to a bubble in commodity prices ---including home heating oil and crude oil --- that peaked in mid-2008. The expanding number of hedge funds and other investors who increased asset allocations to commodities also put upward pressure on prices. Notably, though, no reliable data about the size or effect of these two influential groups has been readily accessible to market participants. I believe the CFTC should promote greater transparency and market integrity by regularly providing the public with better data regarding the role of non-commercial traders in energy and other markets.

If confirmed, I will work with the Congress to provide the CFTC with the additional authority it needs to improve the transparency of the OTC derivatives market. I will also work with the CFTC staff to use the tools at the agency's disposal to protect consumers, investors, and farmers by promoting transparency through more sophisticated data collection and dissemination.

2. Establish conflict of interest rules and firewalls limiting energy infrastructure affiliates from communicating with energy analysts and traders.

I believe we need to adopt a comprehensive plan for the regulation of over-the-counter derivatives markets. As a key component of this reform, we should subject all derivatives dealers to:

- conservative capital requirements;
- business conduct standards;
- record keeping requirements (including an audit trail);
- reporting requirements; and
- conservative margin requirements.

The CFTC should have the authority to protect against fraud, manipulation, excessive speculation, and other market abuses within the OTC derivatives markets, including all energy derivatives, and by the derivatives dealers.

Working with Congress, such authorities to subject dealers to business conduct standards and to protect against market abuses could include the establishment of rules relating to conflicts of interest. If confirmed, I look forward to working with other Federal agencies and the Congress to achieve these objectives.

3. (a) Work with the Federal Reserve to prohibit bank holding companies from trading in energy commodity derivative markets and owning energy infrastructure assets.

Given the recent changes in the structure and composition of the financial and energy industries this is an important issue. Generally, I believe the CFTC must be ever vigilant in its oversight to protect the public against fraud, manipulation, excessive speculation, and other market abuses in the energy, agricultural and financial commodity markets. As described in my answers above, we need to adopt a comprehensive plan for the regulation of over-the-counter derivatives – including those trading energy derivatives. This should subject all dealers, including those held by bank holding companies, to a robust regime of prudential supervision and regulation. More specifically, I believe that derivatives dealers, including those held by bank holding companies, should be subject to business conduct standards as described in Question 2, and speculative position limits as described below in Question 3(b).

If confirmed, I look forward to working with the Federal Reserve, other regulators, the Administration, and the Congress on this important issue.

(b) The CFTC should promulgate rules to make sure that all bank holding companies that engage in derivatives trading are subject to speculation limits.

A transparent and consistent playing field for all physical commodity futures should be the foundation of the CFTC's regulations. Position limits must be applied consistently across all markets, across all trading platforms, and exemptions to them must be limited and well defined.

As part of the comprehensive plan described above, the CFTC should be provided with authority to set position limits on all OTC derivatives to prevent manipulation and excessive speculation. Such position limit authority should clearly empower the CFTC to establish aggregate position limits across markets in order to ensure that traders are not able to avoid position limits in a market by moving to a related exchange or market.

If confirmed by the Senate, I will ask the CFTC staff to undertake a review of all outstanding hedge exemptions, to consider the appropriateness of these exemptions, and to evaluate potential practices for instituting regular review and increased reporting by exemption-holders.

4. Mr. Gensler should work to promulgate regulations within 3 months to require hedge funds that are engaged in derivatives trading to register with the CFTC.

The Administration has proposed that all advisers to hedge funds (and other private pools of capital, including private equity funds and venture capital funds) whose assets under management exceed a certain threshold should be required to register. If confirmed, I will work closely with Congress to pass legislation that will mandate registration of hedge fund advisers as part of a comprehensive package of regulatory reform. In addition, if confirmed, I will work with the agency staff to review all previously granted exemptions from registration as commodity pool operators.

Furthermore, as part of the comprehensive reform of the derivatives market, the CFTC should have the authority to police all activities in the OTC derivatives markets—including transactions entered into by hedge funds. If confirmed, I look forward to working with other Federal agencies and the Congress to achieve these objectives.

6. Mr. Gensler should support revoking all “no-action” letters for Foreign Boards of Trade that solicit or accept business from the U.S.

I support actions to close the “London Loophole” and ensure that foreign futures exchanges with permanent trading terminals in the U.S. comply with the position limitations and reporting and transparency requirements that are applied to trades made on U.S. exchanges. Furthermore, I believe any foreign futures exchanges that have terminals in the United States to which our investors have access and whose contracts are based on the same underlying commodities should have consistent regulation applied, including position limits.

If confirmed by the Senate, I look forward to working with Congress to give the CFTC unambiguous authority to promulgate rules and standards to achieve these goals. Such rules and standards governing treatment of Foreign Boards of Trade should replace the issuance of “no-action” letters in this regard.